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Taxation of the extractive industries

Subcommittee on Extractive Industries Taxation Issues for Developing Countries

Note by the Secretariat

Summary

The present note provides a historical perspective on the current status of the discussions on the taxation of extractive industries. It summarizes the discussions leading up to the establishment of the Subcommittee on Extractive Industries Taxation Issues for Developing Countries and the work that the Subcommittee has carried out since its inception.

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Introduction

1. The taxation of the extractive industries has become a priority of the Committee of Experts on International Cooperation in Tax Matters. The issue arose during the eighth session of the Committee, and a subcommittee was formed at its ninth session.

Eighth session of the Committee (2012)

2. At the eighth session, and building on a prior presentation on the use of tax incentives by Stefan van Parys,[1] Robin Oliver (then a member of the Committee) gave a presentation[2] on how the taxation of foreign capital negatively affects the volume of investment, resulting in lower wages and/or higher unemployment. Discussions were held on issues of location-specific economic rents and their relevance to articles 5 and 7 of the United Nations Model Double Taxation Convention between Developed and Developing Countries, on permanent establishment and business profits, respectively; article 6, on income from immovable property; article 9, on associated enterprises; article 10, on dividends; article 11, on interest; and article 12, on royalties.

3. Following Mr. Oliver's presentation, the Committee discussed issues such as location-specific rents associated with natural resources and the need for appropriate tax policies for resource exploitation. According to a number of participants, many developing countries were losing out on such revenue. Those exploiting the resources were often provided with tax exemptions that could not be economically justified, while their activities led to externalities, for example environmental damage, that negatively affected local communities, which were often not appropriately compensated. Owing to the importance of the issue, the Committee decided that its work on it should continue and that a working group should be formed. However, since the four-year terms of the current membership of the Committee had concluded, the formation of such a working group was deferred to the new membership.

Expert group meeting (May 2013)

4. With a view to assisting the Committee in addressing the agenda item, the Financing for Development Office of the Department of Economic and Social Affairs organized a one-day expert group meeting on 28 May 2013. The discussions focused on the issues that developing countries faced when designing and administering an extractive industries fiscal regime, with a view to ensuring that the tax cooperation work of the United Nations could further support developing countries in that important area of development. During the meeting, participants from national tax authorities, international organizations, non-governmental organizations and the private sector considered the question of international tax cooperation in the extractive industries sector, including institutional arrangements

[1] Available from www.un.org/esa/ffd/tax/sixthsession/UseOfTaxIncentivesALL.pdf.
[2] Available from www.un.org/esa/ffd/tax/eighthsession/PPTs/PPT_CRP11.pdf.

to promote such cooperation. Summaries of the presentations of the participants and the ensuring discussions are contained in a detailed report of the meeting.[3]

Ninth session of the Committee (2013)

5. At the ninth session, the new membership of the Committee decided to form a Subcommittee on Extractive Industries Taxation Issues for Developing Countries with the mandate to consider, report on and propose draft guidance on extractive industries taxation issues. In undertaking its work, the Subcommittee would seek to engage with other organizations that are active in the field. The Subcommittee would comprise representatives from tax administrations having wide and varied experience in dealing with the extractive industries; academia; international organizations; and the private sector, including from petroleum and mining companies.

Subcommittee on Extractive Industries Taxation Issues for Developing Countries

First meeting of the Subcommittee

6. The initial meeting of the Subcommittee, hosted by the South African Revenue Service, was held in Johannesburg, South Africa, in May 2014. Sixteen Subcommittee members participated, representing Governments, business, academia, and regional and international organizations. The main outcome of the meeting was an agreement to focus on areas where the United Nations could add special value, while also drawing upon the work of regional, international and other organizations. The goal was to publish an overview note on issues in that area as well as more detailed policy and administrative guidance notes that focused on the specific taxation and governance aspects of the extractive industries. This included capital gains tax issues in that area, including offshore "indirect" sales of local assets, environmental reclamation, tax treaty issues and value added taxation.

7. Some of the other topics discussed, with a view to deciding on the areas of greatest relevance, included:

- Capital gains taxation of assets in the extractive industries
- Tax treatment of environmental reclamation and rehabilitation
- Double taxation treaty issues
- VAT issues
- Tax incentives applying to the extractive industries
- Tax issues related to price fluctuations
- Ring-fencing issues
- Taxation of service providers to the extractive industries
- Knowledge gap issues
- Windfall taxes

[3] Available from www.un.org/esa/ffd/tax/ninthsession/CRP19_ExtractiveIndustries.pdf.

Second meeting of the Subcommittee

8. The second meeting of the Subcommittee, hosted by the Tanzanian Revenue Authority, was held in Arusha, United Republic of Tanzania, in August 2014. First drafts of various policy and administrative guidance notes were discussed by the members of the Subcommittee.

9. The Subcommittee decided that:

- It would put before the Committee at its tenth session, in October 2014, draft guidance notes or outlines (as appropriate in each case and where possible in respect of relevant time frames) on capital gains on indirect sales, tax treaty issues, certain VAT issues and the tax aspects of decommissioning of extractive projects
- It would also provide the Committee with an outline of a proposed overview note to accompany the specific guidance notes
- In accordance with its mandate, it would provide a work programme for the Committee at its 2014 session that would incorporate other guidance notes proposed for the Subcommittee's focus in 2015 and outline other possible topics for guidance in future years.